IRREGULAR ASSOCIATIONS.

PART III.

IV. AMENABILITY TO SUIT IN THE COMMON NAME.*—This question is obviously connected closely with the problem last discussed.[1] The difference is that where the associates are suing the question is whether their irregular organization is fatal to the privilege claimed. Where they are being sued the question is whether they may set up the irregularity in their own defence. As the decisions show that the associates may exercise the privilege in the former case, it is natural to find that in the latter case the authorities discountenance the defence. Sometimes the contract theory is invoked. More often it is said that the associates are "estopped."[2] "Objections like these are certainly not to be favored when made by a company holding themselves out as a corporation and contracting liabilities as such."[3] Sometimes the question is discussed as if the problem concerned the burden of proof. In such cases it is said that "it is not incumbent on the plaintiff to prove that the defendants have complied with the requisitions of the statutes. . . . The existence of a corporation, and, of course, its organization, may be proved by reputation, and by its actual use, for a length of time, of the powers and privileges of a corporation."[4] In this branch of the subject, as in others, the case which strains conventional explanations to the breaking point is the case in which associates are sued in the common name for a *tort*. An important case of this class is the decision of the House of Lords in *Taff Vale Ry.*

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* The two preceding articles in this series have discussed the effect of irregular corporate organization upon (I) the liability of the associates; (II) their right to act in the common name; and (III) their right to sue in the common name.

[1] To wit, the right of associates irregularly organized to sue in the common name.

[2] See, for example, *Collender* v. *Painesville, etc., R. R. Co.*, 11 Ohio St. 516 (1860).

[3] Dewey, J., in *Dooley* v. *Cheshire Glass Co.*, 15 Gray, 494 (1860).

[4] Shaw, C. J., in *Narragansett Bk.* v. *Atlantic Silk Co.*, 3 Metc. 287 (1841).

Co. v. *Amalgamated Soc. of Ry. Servants.*[5] The railway had obtained from Farwell, J., an injunction against the Servants to restrain them and their agents from watching and besetting the plaintiffs' works and from persuading or endeavoring to persuade persons under contract with the plaintiffs to leave their employ. The injunction was granted on a summons directed against the Servants in their common name. To this name the Servants had acquired an exclusive right by registration under the Trades Union Acts. These acts confer the privilege of holding property in the common name but do not expressly confer the right to sue or to be sued therein. On appeal from the refusal of a motion to strike out the name of the Servants from the injunction order, the Court of Appeals reversed the decision of Farwell, J., and their judgment was in turn reversed on appeal by the House of Lords. All the judges in all the courts, without, apparently, any clear idea of what a corporation is, were of opinion that the trades union in question was not made a corporation by the acts of Parliament. Farwell, J., and some of the judges in the House of Lords thought that the intention of Parliament to make the Servants amenable to suit in the common name was a fair inference from the provisions of the acts. Lord Halsbury regarded the implication of liability to suit as a consequence of the privileges conferred upon the Servants by the acts. Lord Brompton thought that "a legal entity was created under the Trades Union Act of 1871 by the registration of the society in its present name in the manner prescribed, and that the legal entity so created, though perhaps not in the strict sense a corporation, is nevertheless a newly created corporate body, created by statute, distinct from the unincorporated trade union, consisting of many thousands of separate individuals, which no longer exists under any other name." [6] Lord Lindley's opinion contains a useful contribution to the discussion. He observes that

[5] 85 L. T. 147 (1901).

[6] This passage is a good illustration of the common confusion of thought involved in treating the existence of the so-called entity as a basis of inference that a given right exists. In point of fact, it is the existence of the right that gives rise to the conception of the entity.

the equity principle which permits some of a class to be sued as representatives of all forbids the restriction of the rule "to cases for which an exact precedent can be found in the reports." "The principle is as applicable to new cases as to old and ought to be applied to the exigencies of modern life as occasion requires." "I have myself no doubt whatever that if the trade union could not be sued in this case in its registered name, some of its members (viz., its executive committee) could be sued on behalf of themselves and the other members of the society and an injunction and judgment for damages could be obtained in a proper case in an action so framed." He then gives his reasons for thinking that Parliament intended to subject the Servants to suit in their registered name.

The ostensible ground of this decision is, as has been seen, an implication of a grant by Parliament of the right to sue the associates in the common name. The real explanation, it is submitted, is the inconvenience and failure of justice which would result from any other conclusion. Lord Lindley frankly says that, in the absence of any statute, a suit should be sustained if brought against the Servants representatively. To recognize the right to obtain relief against all where some only are joined, differs little from a recognition of the principle that a summons in the common name served on a representative is a command to all the associates to appear. When the appearance is finally entered, it is an appearance by counsel on behalf of all. The fact that compels the recognition of the right is the fact that the Servants have actually associated themselves as a large group organized on representative principles and are acting in corporate form. They are in fact incorporated and must be treated accordingly. It will, of course, be observed that the case under discussion involves no question of irregular organization. It is, however, the case of incorporation without statutory authority.

V. Conveying and Receiving Title to Property.—Unless the situation is complicated by the existence of a recording system there seems to be no reason why co-owners of property should not give and receive conveyances in the

common name by which they have elected to be known. The document which evidences the transaction will contain the common name as the designation either of the grantors or grantees. If the associates are the grantors, a representative must act on their behalf in executing the document of title and in making delivery of it. The right thus to make use of a common name is a right which ought perhaps to be regulated by statute in the interest of public convenience, but if associates claim the right and actually exercise it, legal effect should be given to the action which they take. The clearest case for the application of this proposition is the case in which the question respecting the effect of the conveyance arises as between the associates and their grantee. Neither the associates nor their grantee should be permitted to repudiate the conveyance or to act in a manner inconsistent with it. Substantially the same question is presented where the attack on the conveyance is made by one who is not a party to it. A conveyed land by deed to persons associated under the common name of the X Co. Thereafter the associates in the common name conveyed the premises to B. A then brought an action against B to recover possession of the land, averring that the associates were not validly incorporated at the time of the conveyance to them in their common name. The court were of opinion that A was estopped by his conveyance from disputing its legal effect.[7] This is, of course, in effect to decide that the conveyance was valid. The court in the course of the opinion intimated that a different result would be reached if the associates had been incorporated under an unconstitutional law. It is conceived, however, that this circumstance would not really be material except upon the fiction theory which assumes the corporation to be a person created by state action. A logical application of the fiction theory necessitates the conclusion that if no corporation was ever created, there could have been no valid conveyance because there was no grantee. An application of this artificial reasoning was made in *Fay* v. *Noble*.[8] C and others undertook to attain incorpora-

[7] *Snyder* v. *Studebaker*, 19 Ind. 462 (1862).
[8] 7 Cushing, 188 (1851).

tion under a general law and C transferred real and personal property to the associates in their common name, receiving payment in shares of stock equal in number to three-fourths of the whole number of shares. C acted as the general agent of the associates and in that capacity borrowed money from A, giving a note signed in the common name and depositing certain personal property belonging to the associates as collateral security for the debt. At this time the organization effected by the associates was irregular, but subsequently they reorganized regularly and conveyed all their property to B by way of mortgage, and B under this mortgage took possession of the property which had been pledged to A. In replevin by A against B it is clear that A was entitled to a favorable decision in case it should be found as a fact that C had the requisite authority to make the pledge. The conveyance of the property by C to the associates in their common name was a valid transfer and the subsequent pledge of the common property by C, if acting within the scope of his authority, gave to A a right which was violated when B took possession under the later conveyance. In point of fact, there was a verdict and judgment for B in the court below, but upon writ of error the appellate court were of opinion that there had been a mistrial and that the verdict should be set aside and a new trial ordered. The result, therefore, was satisfactory because the finding that C lacked authority to make the pledge would appear to have been contrary to the evidence. It is worth while, however, to examine the reasons which influenced the action of the trial judge and the appellate court. The trial judge was of opinion that at the time of the pledge to A there had been no valid incorporation. The associates, he thought, were not necessarily partners, and it was a question for the jury to determine what the agreement actually was under which they were doing business. From a consideration of this agreement the jury were to infer what was the scope of C's authority to act for his associates and to determine whether or not he had the right to pledge the common property to secure the indebtednes to A. If the view of the trial judge is open

to criticism at all, it is upon the ground that he ought to have directed a verdict for A on the ground that C's authority to make the pledge should be determined by the court from an inspection of the articles of association, minutes, and other documents offered in evidence. The appellate court, however, took an entirely different view. In the opinion of Bigelow, J., if associates fail to attain valid incorporation they are not partners although they carry on a manufacturing business for the sake of profit. If, therefore, the trial judge was correct in deciding that there was no valid incorporation at the time of the pledge, there was a total failure to create a corporation, since "corporations are known and recognized legal entities with rights and powers clearly defined and well understood and wholly distinct and different from those of individuals and co-partnerships." As there was no corporation, C had no principal; for he had no authority to act on behalf of the individual associates. If he had no principal, he was not an agent. "If he purchased, he purchased for himself. In him only did the property vest, and as against all but the vendors he had the sole right to dispose of it to others." From this it would follow that the pledge to A was valid, not because C was making an authorized disposition of the common property, but because he was dealing with his own property. It would be difficult to think of a more artificial method of arriving at an obviously sound result.

A problem not essentially different from those that have been discussed is presented when a subsequent mortgagee undertakes to question the validity of a prior mortgage on the ground that the holders of the mortgage are not validly incorporated. C mortgaged real estate to B, a corporation *de facto,* and subsequently mortgaged the same property to A. A in a proceeding to foreclose his mortgage contended that the prior mortgage to B was invalid by reason of irregularities in the organization of B. It could not be said in such a case that A was estopped, nor was he a party to any contract by which corporate rights of the holders of the first mortgage were recognized. Since, however, the conveyance had actually been made to the associates

in the common name there was no reason why effect should not be given to it. The court accordingly declined to treat the first mortgage as void and recognized the legality of the conveyance to the associates in their common name by making use of the familiar statement that its legality could not be questioned collaterally. This, as has already been so often pointed out, is the same thing as saying that legal effect will be given to the act which has been done. "This rule," said the court, "is not limited to cases where one by contract admits corporate existence, but is a rule of general application." [9]

As associates may by organizing themselves in corporate form attain the right to make and receive conveyances in the common name, it should follow that a conveyance actually made in the exercise of such right should not be invalidated by a subsequent judgment of ouster pronounced against the associates because of their unlicensed exercise of corporate rights. Persons associated under the name of X gave a mortgage to A. Subsequently they gave to B and others associated in corporate form a deed purporting to convey to the grantees in their common name the premises theretofore mortgaged to A. X subsequently made various other conveyances of portions of the land in question. The mortgage to A was, however, not recorded by A until after all the other conveyances which have been mentioned. A then brought an action to foreclose the mortgage as against the grantees, mortgagees, and purchasers who had acquired their rights prior to the recording of A's mortgage. Among the defendants were B and associates in their common name. During the pendency of the foreclosure suit *quo warranto* proceedings were instituted by the attorney-general against B and associates and a decree of ouster was rendered on the ground that they had never attained legal incorporation. At the trial of the foreclosure proceedings the record of the *quo warranto* proceedings was admitted in evidence and the court refused to allow B and associates to prove that they had in fact attained

[9] *Williams* v. *Kokomo B. and L. Ass'n*, 89 Ind. 389 (1883).

corporate organization. The judgment rendered in favor of the plaintiff was reversed.[10] in the course of a careful opinion by Owen, J., the following language occurs: "The theory that a *de facto* corporation has no real existence, that it is a mere phantom, to be invoked only by that rule of estoppel which forbids a party who has dealt with a pretended corporation to deny its corporate existence, has no foundation either in reason or authority. A *de facto* corporation is a reality. It has actually a substantial legal existence. It is, as the term implies, a *corporation.*"

It is submitted that the decision in *Perun* v. *Cleveland* was clearly correct and that the opinion is a substantial recognition of the fact that corporate rights may be attained by associates without state grant and that acts done in the exercise of those rights will be accorded their ordinary legal consequences. It is, of course, entirely consistent with this view that the state should be free to discipline the associates for having exercised without license rights which it is to the public interest to regulate and control.

VI. Effect of Irregularities upon the Relation of Associates Inter Se.—Let it be supposed that associates unite in organizing in corporate form but fail to comply with one of the requirements of the general law. After the business has been conducted for some time a dispute arises between the associates respecting the management of the concern and one of them files a bill against his associates seeking to have the association declared a partnership and to have a settlement of its affairs on partnership principles. The question is whether the complainant may thus ignore the character of the organization which has been effected and treat the group as if organized on a partnership basis. On principle it should seem clear that the associates have in fact become incorporated and that no one of them is entitled to invoke any remedies except such as are available to corporate members.

The facts of the suppositious case just stated are substantially those of *Bushnell* v. *Consolidated Ice Machine*

[10] *Society Perun* v. *Cleveland,* 43 Ohio St. 481 (1885).

Co.[11] In that case it appeared that subsequent to the beginning of business and to the plaintiff's participation therein he had temporarily lost his reason and that his associates had caused his stock in the company to be sold for non-payment of installments. After his restoration to health plaintiff was excluded from all share or participation in the management of the business. To a bill filed to have the association declared a partnership the defendants demurred. The demurrer was sustained and on appeal the decree was affirmed.[12]

SUMMARY.

The conclusion of the whole matter is submitted to be as follows:

1. Two or more persons may without state license cause action to be taken on their behalf in a common name or action may be taken against them in that name. The question whether legal effect shall be given to such action is distinct from the question whether or not the associates are liable, with or without limit, for the action so taken if legal effect is given to it.

2. Whether or not the associates who thus attempt collective action without state license are *incorporated* depends *first,* upon whether they have so organized their group that nothing but collective action by official representatives is possible; and, *second,* upon whether full effect will be given to an unlicensed representative organization wherever the state it not a party to the proceeding. If either question is answered in the negative, the associates are not incorporated.

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[11] 138 Ill. 67 (1891).

[12] A question analogous to that just discussed is presented when one of two associates seeks a partnership remedy against the other on the ground that the acquisition of all the shares of stock by two persons effects the dissolution of the corporation. In *Russell* v. *McLellan,* 14 Pick. 63 (1833), the plaintiff in a partnership bill for an account contended that in framing a corporation law the legislature contemplated the association of at least three persons to the end that disputed questions might be decided by a majority vote. The court was of opinion that the corporation had not been dissolved. The associates were not, therefore, "partners, joint tenants, or tenants in common" within the meaning of a Massachusetts statute (St. 1823, c. 140) conferring equity jurisdiction upon the court, and the bill was accordingly dismissed.

3. Whether or not legal effect shall be given to the particular kind of collective action attempted in any given case is a question which does not necessarily involve the inquiry whether the associates are fully incorporated. The concession of legal validity to a single form of collective action need not imply a similar concession as respects other forms.

4. The conception of limited liability as an incident of incorporation results from the development of the idea of corporate personality; and this idea is, in turn, the consequence of completely eliminating individual action and substituting collective action. To concede limited liability to the members of an unlicensed group implies that all the modes of collective action are likewise conceded. Such a concession is, therefore, equivalent to an admission of the possibility of incorporation by the private act of the associates.

5. As a corollary to (4) it follows that if incorporation without license is recognized as legally effective, though irregular, there need be no hesitation in according legal validity to acts done in the common name by associates irregularly organized. The same conclusion is applicable as respects suing and being sued in the common name and making and taking conveyances of property.

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